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Rodd Zolkos

# Captive insurance market grows as economy recovers

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The global captive insurance market continued to grow in 2012, both in terms of new captive formations and new captive domiciles. New captive insurers are forming to provide a variety of coverages for a host of different industries, with particular activity in formations by health care organizations or formations of group captives to provide stop-loss coverage for employee medical benefit programs.

Worldwide, the number of licensed captives increased to 6,052 at the end of 2012 from 5,807 a year earlier, according to the annual Business Insurance survey of captive domiciles.

The world's three largest captive domiciles were unchanged at the end of last year, with Bermuda with 856 captives, the Cayman Islands with 741 and Vermont with 586. The Cayman Islands also was among the domiciles licensing the most new captives in 2012 with 53, while Vermont licensed 32.

Other domiciles also had active years, including Utah with 68 new captives and Delaware licensing 59.

“Competition between the domiciles is more intense than ever,” said Brady Young, president and CEO of Strategic Risk Solutions Inc. in Concord, Mass. “I think some of the upstart domiciles are aggressively looking to grow and are not happy or willing to take a back seat to Vermont or Cayman or other well-established, mature domiciles.”

While new captive formations continued at a healthy pace around the world in 2012, the number of captives being dissolved kept the worldwide total from being even higher. In the Cayman Islands, for example, 51 captives were dissolved last year, while in Vermont there were 36 dissolutions.

In Vermont, the result was that while 2012 “was a very good year” in terms of new formations with 32, overall “we actually lost a net four,” said David F. Provost, deputy commissioner of the Captive Insurance Division in the Vermont Department of Financial Regulation.

“Most of the dissolutions were due to merger and acquisition activity” and the merged parents finding themselves with multiple captives, Mr. Provost said. Also, Vermont has been encouraging owners of dormant captives to either make use of them or close them down, he said.

Captives move back onshore usually because of cost, Mr. Provost said. “They get a little bit of a perception issue, but it usually comes down to they no longer need to be there and it makes more sense for them to be onshore.”

“I don't see any great drive to move off the islands,” Mr. Provost said. “It's such a mature business now that people are going to move and do what's best for them.”

Of the captives that left Vermont for other domiciles, Mr. Provost said, “We think some of those were directly related to Dodd-Frank self-procurement taxes. And some of those were just that they now have a home-state option. Sometimes politics enters into it.”

“As all the states pass laws — and they're all pretty similar laws — I think it's going to be harder for us to differentiate ourselves and we're going to have to focus on client service,” said Mr. Provost. “We're focusing now on the efficiency of our exams.”
Andrew Sargeant, chief operating officer at USA Risk Group Inc. in Montpelier, Vt., said he doesn't think regulatory differences are driving captive owners' domicile choices.

“I think it's other factors,” he said. In some cases, he said, it's been issues with parent companies' home states' interpretation of the Nonadmitted and Reinsurance Reform Act of the Dodd-Frank Wall Street Reform and Consumer Protection Act (see story page 22). “I think geographic reasons and not having to travel far has a little to do with it as well,” he said.

Mr. Sargeant said he's uncertain whether the new domiciles coming on the captive scene will achieve critical mass and truly compete with the world's largest domiciles. “We did one in Oklahoma last year, and we did one in New York last year,” he said. The new domiciles will “get a few, but whether they'll ever get more than 100, I don't know.”

The captive market also is showing signs of a strengthening global economy. “We had five businesses in the construction industry form captives this year,” Mr. Provost said. “That's a good sign of a potentially recovering economy, and that's what we got when we talked to those folks — things were looking up.”

“We still have a lot of interest all over the map and all kinds of activity,” said Les Boughner, managing director of Willis Group Holdings P.L.C.'s North American captive practice in Burlington, Vt. “We still see interest in TRIA captives. Cyber comes up all the time, but I don't think we've actually done one. We're still seeing a lot of workers comp, still seeing 831(b)s forming.”

Last year's 18 risk retention group formations across the U.S. represented the highest level since 2007. Around the country, some states continue to engage in regulatory disputes with RRGs over issues of contract liability, however, said Robert H. Myers Jr., partner at Morris, Manning & Martin L.L.P. in Washington. “The same kind of sniping that goes on from some states is continuing,” Mr. Myers said. “We'll see how these disputes evolve.”

A significant RRG case that is in the courts — stemming from Nevada's effort to block the Alliance of Nonprofits for Insurance, Risk Retention Group from writing first-dollar auto coverage in the state — was heard by the 9th U.S. Circuit Court of Appeals in San Francisco in February after a lower court ruled in 2011 that federal law pre-empted the state's efforts. There's no indication of when the appeals court will rule on the case.

Also on the captive regulatory front, the industry continues to be interested in the European Union's pending Solvency II regulatory regime. While the enactment of Solvency II is now expected in 2016, those in the captive industry continue to monitor developments regarding possible impacts on captives. And while it's a European initiative, with pressure for international standardization of insurance regulation, it ultimately could have an effect on U.S. captives, Mr. Myers said.

“I think the U.S. is still keeping it at arm's length, but you never know. We have this unusual regulation system where peer pressure counts sometimes more than what the law says,” he said.